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Inflation Protection and the Anti-Inflation Regulations

Louis ASCAH

This note examines the inflation protection provided by the Anti-Inflation Regulations.¹ It is assumed that the correct number for real compensation increases is 2 per cent per annum as provided in the guidelines for the national productivity factor.^{2,3}

By full inflation protection we mean protection not only of the initial level of real compensation but also of the appropriate increase, if any, in real compensation. If inflation protection is limited only to ensuring that the total rate of increase in compensation just matches the rate of inflation it is implicitly assumed that no increase in real compensation is appropriate.

Accordingly table 1 presents the realized October to October increase in the consumer price index and the annual increase required for full inflation protection (calculated and defined as 2 per cent plus the realized inflation rate).⁴ Since the realized inflation rate is not known beforehand, this full inflation protection can be provided by granting an initial increase on the basis of a predicted rate of inflation and, ex-post, granting a retroactive increase or a lump sum retroactive payment on the basis of the difference between the realized rate of inflation and the predicted rate.⁵

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1 This note refers to the basic increases allowed by the Regulations (basic protection factor and national productivity factor) and does not take into account the experience adjustment factor or other special consideration factors. See Anti-Inflation Board (1975) hereafter cited as *Regulations*.

2 *Ibid.* section 47. Also see Government of Canada (1975: 21).

3 In fact a very strong case can be made to show that the 2 per cent per annum national productivity number is biased downwards. See INGERMAN and ROSE-LIZÉE (1977).

4 Similar reasoning as to inflation protection was used by the Honourable Emmet Hall, arbitrator, in commenting on the increases provided by Parliament to railway workers under the Maintenance of Railway Operations Act, 1973. He wrote: "If the 8% increase granted in Bill C-217 for 1974 is taken as being related almost exclusively to the cost of living factor, then Parliament really made no provision in respect of productivity in which the employees might be expected to participate in or, on the other hand, if any substantial part of the 8% was to be allocated to productivity then the balance left to be allocated to cost of living increase was not adequate because the total of the two components exceeds 8%". Government of Canada (1974: 31).

5 Such a retroactive increase was provided for in the Quebec public sector collective agreements (1972-1975). See ASCAH and INGERMAN (1974).

TABLE 1

**Rates of Increase in the Consumer Price Index Increases in
Compensation Required for Inflation Protection and
Increases Allowed by Anti-Inflation Regulations.
1975-1978**

| | <i>Realized increase in Consumer Price Index</i> | <i>Initial Portion of Basic Protection Factor</i> | <i>Increase Required for full inflation protection</i> | <i>Increase allowed by ori- ginal re- gulations</i> | <i>Increase allowed by revised regu- lation</i> |
|-----------------------------------|--|---|--|---|---|
| First Program Year | 6.2% | 8% | 8.2% | 10% | 10% |
| Oct. 14, 1975 to Oct. 13, 1976 | | | | | |
| Second Program Year | 8.8% | 6% | 10.8% | 8% | 8% |
| Oct. 14, 1976 to Oct. 13, 1977 | | | | | |
| Third Program Year | 8.7% | 4% | 10.7% | 8.8% | 6% |
| Oct. 14, 1977 to Oct. 13, 1978 | | | | | |
| Total compounded increase | 25.6% | — | 32.7% | 29.3% | 25.9% |

Source: See Text.

The original anti-inflation regulations provided that any excess of the increase in the consumer price index over the initial increase provided for in the basis protection factor for that year may be included in the allowable compensation increase of the following year.⁶ However, the regulations did not provide for a retroactive payment and on this basis there is a difference between the increase allowed by the original regulations and the increase required for full inflation protection as shown in table 1.⁷ In the first program year where the realized inflation rate (6.2%) was lower than the initial portion of the basic protection factor (8%), the increase allowed by the original regulations was (10%) was higher than the increase required for full inflation protection (8.2%). Of course the opposite result prevailed in the second and third program years.

⁶ Regulations section 46.

⁷ In fact this type of retroactive protection was eventually explicitly effectively denied. "The permissible increase for a group must not be exceeded in the latter part of a guideline year as a result of the implementation of a triggered COLA formula. If such a cost of living formula were to result in payment of an amount in excess of the permissible increase for the group another element of compensation must be reduced to offset the payment". Anti-Inflation Board (1978).

TABLE 2

**Average annual earnings and difference in average annual earnings
— Industrial Composite — on the basis of increases in compensation
required for inflation protection and increases allowed by
Anti-Inflation Regulations.
1975-1978**

| | <i>Average annual earnings required for full inflation protection</i> | <i>Average annual earnings with increases allowed by original regulations</i> | <i>Average annual earnings with increases allowed by revised regulations</i> |
|--|---|---|--|
| October 1975 | \$11,071 | \$11,071 | \$11,071 |
| First Program Year Oct. 14, 1975 to Oct. 13, 1976 | \$11,979 | \$12,178 (+ \$199) | \$12,178 (+ \$199) |
| Second Program Year Oct. 14, 1976 to Oct. 13, 1977 | \$13,273 | \$13,152 (-\$121) | \$13,152 (-\$121) |
| Third Program Year Oct. 14, 1977 to Oct. 13, 1978 | \$14,693 | \$14,310 (-\$383) | \$13,941 (-\$752) |
| Total difference | | (-\$305) | (-\$674) |

Source: Based on increases contained in table 1 (see text for more details) and on average weekly earnings — industrial composite — October 1975.

Later even the partial protection provided by the original regulation was dropped when the government announced revised regulations for the third program year. The Government revoked the adjustment provision that was to apply because the consumer price index had risen by more than the basic protection factor in the second year and determined that the basic guideline for compensation increases in the third program year would be 6 per cent.⁸ References to the basic protection factor and the national produc-

⁸ The Honourable Jean Chrétien, Minister of Finance justified this change partly as follows: "If we had left the Regulations unchanged, the guideline would have been about 8 per cent because the consumer price index has gone up by more than the price target this year. But I would like to emphasize that the first two years of the Program taken together were just about on target. We did better than the target by almost 2 per cent in the first year and seem likely to fall short by about the same amount in the second year". Government of Canada, Finance (1977). In fact the program did better than the target by 1.8 per cent in the first year and fell short by 2.8 per cent in the second year.

⁹ The average weekly earnings — industrial composite — for October 1975 were \$212.90. *Statistics Canada* (72-002, 1978). Since the regulations apply to compensation it would be preferable to use average weekly compensation data rather than average weekly wages. However such data is not published.

tivity factor for the third program year were deleted. The increases allowed by the revised regulations are also shown in table 1. Over the three years of the Anti-Inflation program the total compounded increase allowed by the revised regulations was 25.9% while the corresponding increase in the consumer price index was 25.6%. This results in a total real increase of less than 0.1% a year in contrast with the initial 2 per cent per annum real increase that was to have been provided for a share in increases in national productivity.

An estimate of the difference caused by the less than full inflation protection of the Anti-Inflation Regulations is presented in table 2. Based on the average weekly earnings for the industrial composite in October 1975, the annual earnings are derived as of that date and for the three program years according to the increases presented in table 1.⁹ Thus a worker earning the average weekly earnings in October 1975 and granted the increases allowed by the revised regulations would have received \$674 less over the three program years than the amount required for full inflation protection.

Thus, the less than full inflation protection of the regulations has meant that there was little or no increase in real compensation over the three program years as compared to the initial statement that the guidelines were to provide 2 per cent per annum for a share in increases in national productivity.

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